

Master Document Audit Program

Activity Code 17900	Defense Security Cooperation Agency (DSCA)
Version No. 4.14, dated November 2015	
B-1	Planning Considerations
Audit Specific Independence Determination	
<p>Members of the audit team and internal specialists consulting on this audit must complete the Audit Specific Independence Determination (w/p 34) prior to starting any work on this assignment.</p> <p><i>(Note: Because staff is sometimes added to on-going audits, supervisors should ensure that all individuals who are directing, performing audit procedures, or reporting on this audit as a member of the audit team who are performing as a consultant have signed this work paper. For example, an FAO may add additional auditors (e.g. FAO technical specialist) to the audit assignment or may need to consult with an internal specialist (e.g., industrial engineers, and operations research specialists) as the audit progresses.)</i></p>	
<p>The Secretary of Defense has designated the Defense Security Cooperation Agency (DSCA) as the director, administrator, and supervisor of the Security Assistance Program. Responsibilities are defined and authorized by the Foreign Assistance Act (FAA) of 1961, as amended; the Arms Export Control Act (AECA), as amended; and other applicable statutes, Executive Orders, and Directives. Foremost of these is the Security Assistance Management Manual, DoD 5105.38-M. Included within the Security Assistance Program is the Foreign Military Financing (FMF) Program, which provides loan and grant financing for Foreign Military Sales and purchases from U.S. firms, which are defined as Direct Commercial Contracts (DCC).</p>	
<p>Under the FMS Program [Ref.: Selected Areas of Cost Guidebook, Chapter 65], the Department of Defense acts as the agent for the purchasing country. These procurements are fully subject to the FAR and audit oversight. However, this is contrasted with DCC procurements, which are between the foreign Government and a U.S. firm -- with the U.S. Government performing reviews, approvals, and audits as a function of providing the financing. DSCA requests that DCAA evaluate the contractor's compliance with the elements of the signed Contractor's Certification and Agreement with Defense Security Cooperation Agency (Certification and Agreement).</p>	
<p>DCCs are agreements between the foreign Government and a U.S. contractor; therefore, they are not subject to the Federal Acquisition Regulation (FAR) or the Cost Accounting Standards (CAS). However, the Certification that DSCA requires all contractors to sign in order to receive financing provides for contractor compliance with certain concepts, procedures and financial constraints that are addressed in the FAR and DCAA's CAM.</p>	
<p>The "Certification Agreement" and the DSCA "Guidelines for Foreign Military Financing of Direct Commercial Contracts" have been revised over time. The latest revision became effective on or about August 2009. (The original certification was dated 1985.) Therefore, the auditor should carefully review the Contractor's Certification to ensure that the appropriate version is being evaluated.</p>	

Master Document Audit Program

Purpose and Scope
This standard audit program assists the auditor in planning and determining if a contractor is in compliance with certain elements of the jointly signed Contractor's Certification and Agreement with DSCA. The program steps should be tailored, as appropriate, and reflect an understanding between the auditor and supervisor as to the scope required.
The purpose of this compliance examination is to determine if the contractor complies with specific elements contained in its signed Contractors Certification and Agreement and report on the contractor's compliance. If the contractor is found to be in noncompliance with any of the certification elements, the auditor is to describe the situation and include the amount of any corresponding/related costs in the report for DSCA's disposition.
Other Planning Considerations
Prior to commencing audit, review guidance that may impact the audit and adjust the scope and procedures appropriately. Guidance to review includes CAM, open MRDs, FAQ training material, guidebooks, etc. available on the DCAA Intranet.
References
<ul style="list-style-type: none">• <i>Guidelines for Foreign Military Financing of Direct Commercial Contracts</i>. This DSCA guideline provides policies and procedures for the use of foreign military financing to fund direct commercial contracts between U.S. industry and the Government of foreign countries. The guidelines serve as a basis for the DSCA review of the foreign Government's request for approval to use foreign military financing to fund direct commercial contracts. The scope of DCAA's evaluation focuses on the contractor's compliance with the signed Certification and Agreement• <i>Contractors Certification and Agreement with Defense Security Cooperation Agency</i>. In consideration of a grant/loan, the contractor agrees to comply with the elements/provisions of the Certification and Agreement. The requirements imposed on the contractor by the Certification and Agreement are contractual and not regulatory.• <i>Security Assistance Management Manual [SAMM], DoD 5105.38-M</i>. This manual provides DSCA's policies and procedures for administering U.S. Military Assistance and Foreign Military Sales Programs and related activities.• CAM 5-600, Audit of Purchasing System Internal Control• CAM 14-908, Compliance Reviews for the Defense Security Cooperation Agency (DSCA)• FAR 3.4, Contingent Fees• Selected Areas of Cost Guidebook, Chapter 65 – Selling Costs

Master Document Audit Program

B-1	Preliminary Steps	W/P Reference
Version No. 4.14, dated November 2015		
1.	Contact the contracting officer to ascertain any known concerns that will impact the audit and adjust the audit scope and procedures accordingly.	
2.	Electronically transmit an acknowledgement/notification to the ACO/Buying Command notifying them of the commencement of the risk assessment and that the expected completion date will be provided in the formal acknowledgement/notification once the risk assessment is complete. (CAM 2-303). The acknowledgement/notification process should be within the timeframe and in accordance with the procedures in CAM 4-104.	
3.	Obtain a copy of the Contractor's Certification and Agreement and relevant correspondence from the contractor.	
4.	Consider audit leads or key prior audit findings from the permanent audit files and prior audits.	
5.	<p>Review permanent file to determine if previous audits included findings and recommendations that impact the subject matter under audit (GAGAS 5.06). If there were findings, auditors should document this information in the risk assessment and perform the following procedures:</p> <ol style="list-style-type: none"> a. During the entrance conference, ask contractor management if corrective actions were taken to address findings and recommendations reported in previous DCAA audits (e.g., questioned costs, business system deficiencies, CAS audits) that are relevant to the subject matter of audit. If yes, have contractor explain corrective actions taken and determine if additional audit procedures should be included in the fieldwork to test the corrective actions. b. Document the results of the inquiry and the impact of the corrective actions to the subject matter under audit. (Note: The purpose of this question is to follow up with contractor on relevant prior DCAA audit findings that could have a material effect on the subject matter of audit.) 	
6.	<p>Review permanent file to determine if the contractor has previously provided other studies or audits (e.g., summary listing of internal audits or external audit reports) that directly relate to the subject matter under audit (GAGAS 5.06). If there are no other studies or audits, document that information in the work papers and perform the procedures below. (If you do not perform the following procedures, you must document your justification for the departure.)</p> <ol style="list-style-type: none"> a. During the entrance conference: <ul style="list-style-type: none"> • Ask contractor management if internal audits were performed. If yes, request contractor provide a summary listing of the internal 	

Master Document Audit Program

<p>audits that would assist us in understanding and evaluating the efficacy of the internal controls relevant to the subject matter of the audit.</p> <ul style="list-style-type: none"> • Ask contractor management if other types of audits or studies were performed by other than DCAA (e.g., other Government audit agencies, consultants, Independent Public Accountants, etc.) that would impact the subject matter under audit. If yes, have contractor explain what type of audits or studies were performed, if there were any related findings or recommendations, and any contractor corrective actions taken as a result. <p>b. If the review of the perm file or the contractor identifies relevant internal audits:</p> <ul style="list-style-type: none"> • Determine if access to these reports is necessary to complete the evaluation of the relevant internal controls to support the risk assessment or audit procedures related to the subject matter of the audit. There must be a nexus between the internal audit reports and the scope of this specific assignment. • Document the results of the determination in writing. • If assignment is at a major contractor location, coordinate with the CAC or FAO point of contact (POC) for internal audit reports to request the contractor provide access to the reports. • If assignment is at a non-major contractor and the FAO does not have a designated POC, the auditor should request the contractor provide access to the internal audit reports. • The request, issued by the CAC, FAO POC or auditor, should include information on how the internal audit report is relevant to the DCAA audit. Place a copy of the request in the assignment administrative work papers. <p>c. If the review of the perm file or the contractor identifies relevant other audits or studies:</p> <ul style="list-style-type: none"> • Obtain publicly available information for the relevant other Government agency audits (e.g., websites for DoD IG or other IGs, service audit agencies, etc.). • Make appropriate adjustments to your risk assessment and planned procedures based on the reported findings. <p>d. Document the results of the inquiries including the response received from contractor's for any request for access to internal audit reports. (If access was not granted this should include the contractor's rationale or justification for not granting access).</p> <p>e. Determine if additional audit procedures are needed to address any identified risk. (Note: The purpose of this question is to discover any new audit leads that could affect the scope of current audit.)</p>	
<p>7. Document the understanding of the contractor's internal controls related to</p>	

Master Document Audit Program

<p>accounting and purchasing systems, particularly as they relate to the Contractor's Certification and Agreement.</p>	
<p>8. Using the framework and the guidelines in WP B-2, obtain and document an understanding of the contractor's internal controls that are relevant to the audit. With the proper planning auditors should be able to obtain and document a major portion of this understanding during a walk-through of the contractor's assertion.</p>	
<p>9. Review the contractor's policies and procedures that describe the process for ensuring compliance with the certification agreement. If the contractor states that written policies and procedures do not exist, request the contractor to prepare a written description of the procedures that are followed. Request the contractor to include references to the company's policies and procedures that mandate the process.</p>	
<p>a. Evaluate the policies/procedures and determine if there are potential internal control weaknesses that could result in noncompliances with the certification agreement.</p>	
<p>b. Determine if the accounting practices applicable to DSCA contracts have adverse cost impacts on the performance of U.S. Government (USG) flexibly priced contracts performed in accordance with FAR and CAS provisions.</p>	
<p>10. During the entrance conference, or other appropriate meeting, make inquiries of contractor management regarding knowledge of any fraud or suspected fraud affecting the subject of this audit, managements awareness of allegations of fraud or suspected fraud affecting this audit, and management's understanding about the risks of fraud relevant to this audit. Note: This discussion and any data submitted should be documented in the working papers.</p>	
<p>11. Based on the team's understanding of the criteria, subject matter, and the contractor and its environment, hold a planning meeting with the audit team (at a minimum, Supervisor and Auditor) to discuss and identify potential noncompliances, due to error or fraud, that could materially affect the subject matter.</p> <p>The discussion should include:</p> <ul style="list-style-type: none"> • relevant prior audit experience (e.g., questioned cost, relevant reported estimating or accounting system deficiencies), • relevant aspects of the contractor and its environment, • risk of material noncompliance due to fraud (e.g., the extent of incentives, pressures and opportunities to commit and conceal fraud, and the propensity to rationalize misstatements), • other known risk factors, 	

Master Document Audit Program

<ul style="list-style-type: none"> • the audit team’s understanding of relevant internal controls, • inquiries to the contractor regarding its fraud management plans and controls. <p>Document fraud risk factor/indicators (see - Sources of Fraud Risk Factors below) that are present and could materially affect the subject matter. If Fraud risk factors are present, document specific audit procedures designed to address the increased risk of material noncompliance due to fraud.</p> <p>Communication among audit team members about the risk of material misstatement due to error or fraud should continue as needed throughout the audit.</p> <p>Sources of Fraud Indicators:</p> <ul style="list-style-type: none"> • GAGAS Appendix Section A.10 – Examples of Indicators of Fraud Risk (http://gao.gov/products/GAO-12-331G) • AU-C 240.A75 (Appendix A)- Consideration of Fraud in a Financial Statement Audit, Examples of Fraud Risk Factors (http://www.aicpa.org/Research/Standards/AuditAttest/DownloadableDocuments/AU-C-00240.pdf) • DoDIG’s Contract Audit Fraud Scenarios and Resources website (http://www.dodig.mil/resources/fraud/resources.html) <p>(To access the Sources of Fraud Indicators, copy and paste the web address shown above into the address block in Internet Explorer.)</p>	
<p>12. Review the contract, contract modifications, and correspondence between the foreign Government, the contractor, and DSCA. Note any special provisions and/or agreements that might affect the items in the certification agreement and the evaluation for compliance.</p>	
<p>13. Conduct an entrance conference. For DCMA requested audits, obtain the contractor’s written consent for release of the audit report or reason(s) for not authorizing release to the foreign Government. Include the release statement as an appendix to the report. If applicable, include a follow up with contractor management on:</p> <ul style="list-style-type: none"> a. corrective actions that address previous DCAA audit findings and recommendations (step 6), b. other studies or audits that impact the subject matter under audit (step 7). 	

Master Document Audit Program

14. Issue a notification letter to the contractor regarding the audit in accordance with CAM 4-302.3.	
15. Summarize the results.	

C-1	Detailed Steps	W/P Reference
Version No. 4.14, dated November 2015		
1.	<u>Elements 6, 7, 8 and 10 -- Flowdown of Terms & Conditions.</u> Contractor agrees to include in subcontracts which are not exempt under paragraphs 6, 7, 8 & 10 of the Certification and Agreement certain written terms and conditions.	
	a. Randomly select from the contractor's records, the names of subcontractors from which significant purchases were made.	
	b. For the subcontracts selected, determine if subcontracts include a clause that authorizes representatives of USG to have access to and the right to examine the subcontractor's books and records for a period of three years after final payment to the contractor. The following subcontracts qualify for an exemption from this clause: <ul style="list-style-type: none"> i. subcontracts equal to or less than \$100,000 in value. ii. all subcontracts if the foreign Government awarded the purchase agreement to the contractor on a competitive lowest responsive bid or best bid/best value basis. iii. subcontracts for common hardware and/or raw materials iv. subcontracts for commercially available U. S. off-the-shelf items v. subcontracts issued and effective prior to date of the Purchase Agreement, that is, the date the Purchase Agreement between the contractor and the foreign government is effective, not the date of the Contractor's Certification and Agreement with DSCA. 	
	c. For the subcontracts selected (except those exempted in 1b. above), determine if the contractor obtained written compliance from its first and second tier subcontractors to the certification signed by the contractor.	
	d. For the subcontracts selected (except those exempted in 1b.v. above) review the terms and conditions of these purchase orders and subcontracts to determine if they include the acknowledgment that USG funds are used for financing.	
	e. For the subcontracts selected (except those exempted in 1b.v. above) determine if subcontracts included the statement that no bribes, rebates, gifts, kickbacks or gratuities were used to secure the contract	

Master Document Audit Program

or subcontract or obtain favorable treatment under such agreements.	
f. Summarize the results.	
2. <u>Elements 9 & 14 -- Commissions & Other Contingent Fees.</u> Contractor certifies that no bribes, rebates, gifts, kickbacks or gratuities, which were intended to secure the Purchase Agreement, have been or will be directly or indirectly offered or given, contrary to U.S. law or regulation.	
a. Request a schedule from the contractor to show the names and amount(s) paid for commissions or other contingent fees to agent(s), broker(s), employee(s), consultant(s) or other recipient(s) for the contract.	
b. Compare the amount(s) obtained in 2.a. above with the information in the certification agreement and determine if the contractor is in compliance.	
c. Review the terms and conditions of the agreements/contracts between the contractor and recipient(s) named in the certification agreement. Determine if the amount paid to date, plus due to be paid through completion of the contract, will result in noncompliance. Reconcile amounts to the contractor's books and records.	
d. Request the contractor to provide the names and amount(s) paid to any other agent(s), broker(s), consultant(s), employee(s), or recipient(s) used to market and/or sell the company's products in the buyer's country. Review the terms and conditions of their agreements and determine if the amount(s) should be included in the schedule for 2.a. above.	
e. Where applicable, request the contractor to furnish the cost for maintaining a sales office in the buyer's country. Evaluate the expenses and determine if any amount(s) should be included in the cost schedule from 2.a. above.	
f. Review the FAO's incurred cost audit files for the contractor and determine if audit data and information (i.e. broker/sales agent(s) commission(s), consultant(s) fees, and employee(s) bonuses) corroborates the contractor's data and information furnished for 2.d. and e. above.	
g. While performing the audit procedures above (2.b. through f.) determine if any costs that are not charged direct to the contract were erroneously charged to flexibly-priced USG contracts.	
h. Determine if the subcontracts selected included a clause that requires the subcontractors to provide the disclosures and certifications set forth in Element 14.c. of the Contractor's Certification and Agreement.	
i. Summarize the results.	

Master Document Audit Program

<p>3. <u>Elements 12 & 13 -- Foreign Content.</u> Contractor certifies that the material or components to be provided under the Purchase Agreement are manufactured and assembled in the U.S., purchased from U.S. firms, and composed of U.S. origin components. Agrees that, if DSCA approves financing of the dollar value of non-U.S. origin components or services stated in the certification, or a specified dollar value of non-U.S. origin content, this value will not be exceeded. The value of raw materials and common hardware items which are procured by a manufacturer from both U.S. and foreign sources and which are not ordinarily segregated by origin, and which are incorporated on an interchangeable basis into the contractor's products, the actual dollar value need not be identified. Instead, a non-U.S. content estimating methodology or system (for example, an annual survey) may be used by the contractor. The use of such a methodology must be approved by DSCA prior to DSCA processing the contract.</p>	
<p>a. Request a schedule from the contractor that shows by supplier(s) [including affiliate(s), segment(s) and/or joint venture(s)] the dollar value for non-U.S. origin components or services and non-U.S. manufactured items and components procured and known or expected to be procured through the time of completion of the contract.</p>	
<p>b. Compare the dollar value for non-U.S. procurements with the amount noted in the certification agreement and determine if the contractor is in compliance.</p>	
<p>c. Evaluate a representative sample of the terms and conditions in subcontract(s), purchase order(s), and other agreements/arrangements for foreign suppliers. Verify that the amount for actual plus scheduled purchases, if any, agrees with the contractor's information provided for non-U.S. procurements.</p>	
<p>d. Test a representative sample for evaluation from appropriate contractor records, subcontractors' and vendors' invoices or billings along with the corresponding bills of lading, and receiving reports.</p>	
<p>e. Determine if the incoming shipments were made from domestic or foreign manufacturers.</p>	
<p>f. Verify the names for shipments made from foreign manufacturers with the contractor's information.</p>	
<p>g. Evaluate contract freight-in costs not evaluated in 3.d. above. Randomly select freight billings and determine if any are for foreign suppliers other than those identified in 3.a. above.</p>	
<p>h. Determine if the contractor maintains a qualified vendor list (QVL). Selectively compare the names of the suppliers for the performance of the contract with the names on the QVL. If significant purchases were made from suppliers that are not listed on the QVL, get an explanation</p>	

Master Document Audit Program

from the contractor.	
i. Review the contractor's documentation for evaluating, screening and selecting the vendors.	
j. Verify that the vendor is a domestic manufacturer (not distributor).	
k. Verify that the vendor is not debarred from doing business with the Government by checking the System for Award Management (SAM) https://www.sam.gov/portal/SAM/#1 ; or the State Department list, http://pmdtc.state.gov/compliance/debar_intro.html . (see CAM 4-711(g) for more information)	
l. If a satisfactory determination cannot be made for the origin of components and services from the audit procedures performed above, consider requesting assistance from the FAO cognizant of the subcontractor, if possible. Our right of access or right to information may be very limited.	
m. Summarize the results.	
4. <u>Element 15 -- Advance Payments.</u> -- Contractor agrees to identify the full amount of any advance payment received under the Purchase Agreement in its accounting records as a down payment, to apply these funds solely to the performance of obligations under this Purchase Agreement, and to provide a clear audit trail on the use of these funds.	
l. Determine from DSCA's contract files the purchase order implementation date between the contractor and buyer (foreign Government). Evaluate the contractor's recorded costs, if any, incurred prior to the purchase agreement implementation date.	
m. Determine if advance payments exceed 15 percent of the contract price.	
n. Selectively evaluate the contractor's subsequent billings and determine if they were made as prescribed in the contract.	
o. Summarize the results.	
5. <u>Element 16 -- Export Transportation.</u> – Agrees that export transportation costs financed under terms of the Purchase Agreement will be paid only to steamship, barge, tug, and airline companies of United States registry.	
l. Determine from DSCA's contract files whether export transportation costs for deliverable contract items are borne by the contractor or buyer (foreign Government).	
m. If export transportation costs are borne by the contractor: Determine from the bill of lading if the transporting carrier(s) country of registry is the United States and whether the cost for shipping is for the defense articles related to this purchase agreement.	
(1) Request from the contractor the name(s) of the transporting	

Master Document Audit Program

carrier(s), the country in which the carrier(s) is registered, and the amount paid to date.	
(2) If the contractor uses freight forwarder(s) to manage exports, obtain their name(s) and the amount(s) paid to date. Evaluate the freight forwarder(s) billing documentation and determine that the contract items were not exported by non-U.S. registered carriers.	
(3) Randomly select and review sales shipping lists (or packing sheets) for contract deliveries. Note the name of the carrier(s) and determine that export transportation was not furnished by non-U.S. registered carriers.	
n. Summarize the results.	
6. <u>Element 17 -- Travel Costs</u> -- Contractor certifies that the cost of travel, per diem, accommodations, lodging, car rental, personal expenses, entertainment, or other similar expenses (except the reasonable cost of business meals) incurred by or on behalf of the purchaser's personnel relating in any way to this contract will be paid by the purchaser, and that these costs will not be financed, in whole or in part, with funds received from the U.S. Government under the Purchase Agreement either directly or indirectly.	
l. Evaluate contract costs for travel, per diem, accommodations, car rental, personal expenses and entertainment and verify that none are for the foreign purchaser's personnel [neither for casual visit(s) nor training under the contract].	
m. Evaluate the FAO's incurred cost audit files for the contractor and determine that there are no travel expense exceptions that pertain to foreign Government personnel.	
n. Summarize the results.	
7. <u>Element 21 -- Penalty, Refund, & Other Reimbursement.</u> Contractor agrees that any penalty payment, refund, or other reimbursement due to the purchaser pursuant to the Purchase Agreement will be paid to the U.S. Government for credit to the FMS trust fund account of the purchaser.	
l. Evaluate the contractor's transaction(s) recorded for penalty payments, refunds, or other reimbursement made to the foreign Government, and determine that the amounts are credited to purchaser's account.	
m. Summarize the results.	

A-1	Concluding Steps	W/P Reference
Version No. 4.14, dated November 2015		

Master Document Audit Program

1. Summarize and document the audit results for supervisory review.	
2. Complete the index and cross-reference the working papers.	
3. Coordinate significant or unusual issues with DSCA. Coordination should be both before and after discussion with the contractor.	
4. Hold an exit conference with the contractor in accordance with CAM 4-304. Discuss any noncompliance issue with the contractor and provide a copy of the draft statement of conditions and recommendations for comments in accordance with CAM 10-210.5.e.	
5. Obtain and review contractor's response. If necessary, revise the audit position supporting the noncompliance.	
6. If the examination discloses information that raises suspicion of fraud or other illegal acts, refer the matter by completing DCAA Form 2000 (see CAM 4-702).	
7. Prepare the draft audit report in accordance with CAM 10-1200. For audits requested by DCMA that have findings of noncompliance, include DSCA Headquarters on distribution. Tailor the report to comply with the contractor's release restrictions, as applicable.	